LIBRARY

MAY 31 1944

The MORTGAGE BANKER

VOL. 5 — No. 9 JUNE, 1944

The Mortgage of Tomorrow

Some people think we need a better mortgage plan for the postwar era; here are some current observations

IF it's true—and hasn't it always been true?—that if you can build a better mousetrap than your competitor, the world will beat a path to your door. And if you have a better mortgage plan than the other boys, you are going to get the loans.

That is about the way a spokesman for one mortgage lending group put it the other day when he was emphasizing to his associates that in the postwar period we may have to do some further streamlining of today's mortgage. Within the memory of most of us now active in the business, we have already done quite a bit of that; but more is to follow, according to many.

New mortgage plans, new ideas for making loans, new protective features, new "liberalizations," and even entirely new conceptions of mortgages as instruments of debt are being suggested on every corner. It is foolish to ignore them. Almost any suggestion for improvement or change is worthy of serious consideration. We have an idea that you are going to hear about many new mortgage plans with the sponsors of each one claiming that at last he has the answer to just what is needed for mortgage financing in the future. Look them over. See what there is in each one that you think the mortgage industry might use.

The savings and loan people, who certainly can't be accused of ever being asleep at the switch, are said to be doing some heavy thinking along these lines. One plan said to have been suggested to them not long ago contemplated a loan of twenty years on a declining interest rate basis. Interest for the first 30 months, according to the proposal, would run around 5.76 per cent, for the next thirty about 5.04 per cent and for the second five years about 4.50 per cent. For the remaining ten years it would be 3.60 per cent.

The difficulty with such a plan, some suggested, was that the higher rate interest would be paid during the early life of the loan so that if the average saving and loan mortgage remained on the institution's book for say around 7½ years only a portion of the borrowers would get the advantage of the low interest for the last ten years. The illustration is significant if only to indicate how our contemporaries are thinking along the line of being able to offer the man who wants to build or buy a home something more than he is offered now.

Members will recall the construction loan plan for Title VI's which W. A. Clarke of Philadelphia described at the MBA Chicago Clinic in March. This was an idea which a New York bank had been toying with and which was aimed at eliminating as much risk as possible in doing business with those builders who aren't good business men—and there are a lot of them as every lender who has done a construction loan business well knows. Members have an outline of this plan in the transcript of the *Construction Loan Procedure* session of that meeting so it isn't necessary to go into it further here.

Another which has attracted considerable attention is the Mortgage Cancellation Plan of Allied Building Credits, Inc., the Weyerhaeuser subsidiary. This idea stems from a desire to eliminate the health factor in mortgage lending, the sponsors believing that this has always been a major hazard in the business. Under this plan, if the husband dies or is totally or permanently disabled, the loan is cancelled. If sickness or injury makes him unemployable "for not less than two weeks, monthly payments are kept up without restitution for as long as one year. At the end of that time, if it is determined that the illness or injury is permanent and that the wage earner can no longer be gainfully employed, the mortgage is cancelled."

In the farm field, the Equitable has a new "Approved Mortgage Plan" which is said to give banks a short-term benefit on long-term loans through a commitment from the company to purchase the loan at the end of the second year, or earlier at the bank's option. The mortgage plan in the farm field

(*Continued page* 8, *column* 1)

Possibly the discussion on the first three pages of this issue may suggest ideas which you have been turning over in your mind about the kind of loan lenders may wish to offer in the future. If so, we would like to hear about them and will see that they get proper attention in subsequent issues.

HOME OWNERS SAFETY LOAN PLAN

Copyright 1944 by F. M. Murphy-R. J. Mitchell

THIS new plan is premised on a borrower-lender psychology heretofore unemployed in the mortgage business and is designed to accomplish the following: (1) Prevent portfolio raiding and loss of prime loans; (2) Stabilize and maintain interest rates; (3) Attract new business and hold old business; (4) Reduce collection and servicing cost; and (5) Prevent premature foreclosures. In addition to these five advantages, the new plan could undoubtedly operate as a smooth-running clutch in shifting from war to peacetime conditions.

What the average borrower wants most in his present day mortgage is a flexibility in the default penalty provision to keep pace with his increasing equity. He likes to feel that he has his loan with a reputable firm that will be lenient with him in case of unavoidable delinquency. But he cannot erase from his mind the fact that he signed legal papers permitting foreclosure action in event monthly payments on the loan become in default. And what puzzles him most is the fact that he remains as vulnerable and exposed to foreclosure after paying off the major part of loan principal, as he was on the day he signed the 15-year note and mortgage.

Thus the thinking borrower is psychologically discouraged from the start. He enters the most important financial transaction of his life with the principals out of tune and out of step along the road to what they both want, namely, orderly repayment of the debt for the mortgagee and for the mortgagor, confidence of being able to some day own his home, free and clear of debt.

This new plan, known as the *Home Owners Safety Loan Plan,* seeks to bring about a cohesion of interests between lender and borrower, much closer than a straight debtor-creditor relationship, so much so, that the longer it exists, the greater the benefits accrue to both parties.

In present-day mortgage practice there is no "hitching post" between the borrower and lender as an incentive to proceed together in the ultimate completion of the original contract. As a result, borrowers are easily lured away by the attraction of some other lender offering a lower rate of interest or other concession.

What the Plan Seeks To Do

The new plan further seeks to cement the lender-borrower relationship on an equitable basis by providing for a better balance of mortgage performance covenants, pointing to a more reasonable equity protection for the borrower; and, in so doing, making it possible for certain benefits to accrue to the lender.

This should be the means of insuring to the lender stable loans at fair interest rates; and to the borrower it should mean a contract capable of fulfillment under reasonable conditions.

The new plan removes the uncertainty of mortgage payment performance by appending a Supplemental Agreement to the mortgage form presently in use. It modifies the penalty default proviso in the basic mortgage and provides for three periods, over the life of the loan, during which the borrower may level off and exercise his right to pay interest and taxes (insurance) only.

The principal deferment periods are defined and established on the Supplemental Agreement when placed in force either on a new or existing loan. Such deferment periods are based on the relationship of original appraised value and reducing principal loan balance.

The first principal deferment period occurs after sufficient monthly payments have been made to reduce the loan principal to a point where at least 50 percent lender protection has been established. The recommended principal deferment periods are for one year each. In the box on this page are

	1st Credit	2d Credit	3d Credit
	After 1st Year	*After 3rd Year*	*After 6th Year*
50 Percent Loan of Appraisal:			
Percent Initial Lender Protection	50.	50.	50.
Percent Principal Reduction	4.5	14.5	31.3
Percent Combined Lender Protection	54.5	64.5	81.3
	After 3rd Year	*After 5th Year*	*After 8th Year*
60 Percent Loan of Appraisal:			
Percent Initial Lender Protection	40.	40.	40.
Percent Principal Reduction	14.5	25.4	44.5
Percent Combined Lender Protection	54.5	65.4	84.5
	After 5th Year	*After 7th Year*	*After 9th Year*
70 Percent Loan of Appraisal:			
Percent Initial Lender Protection	30.	30.	30.
Percent Principal Reduction	25.4	37.5	50.9
Percent Combined Lender Protection	55.4	67.5	80.9
	After 6th Year	*After 8th Year*	*After 10th Year*
80 Percent Loan of Appraisal:			
Percent Initial Lender Protection	20.	20.	20.
Percent Principal Reduction	31.3	44.5	58.1
Percent Combined Lender Protection	51.3	64.5	78.1

Normal depreciation of security properties not considered on this chart because of limited space.

shown the three periods on a 15-year loan at 5 per cent interest, based on the percentage of original loan amount to appraisal.

The originators of the *Home Owners Safety Loan Plan* have worked out similar charts showing Safety Zones for loans of various rates of interest.

The principal deferment periods are designed to be cumulative and are earned by virtue of perfect payment performance for the 12 months immediately preceding the deferment period stipulated on the Supplemental Agreement. It is assumed that borrowers will regard such earned rights with the same conservative respect and caution as they esteem the borrowing privilege of their life insurance policies, namely, a reserve to be tapped only as a last resort.

No extraordinary concession is actually given by the lender because the first principal deferment period would not occur until the lender protection had developed to a point where, under former normal conditions, a straight 5-year loan would have been warranted.

Benefits To Lender

Portfolio raiding would be reduced substantially because accumulated credit reserves would retard competitive loan transfers. Borrowers would not likely be enticed to refinance elsewhere at the sacrifice of earned credit accumulations.

Due to the fact that earned rights are transferable, there would be less likelihood of losing a prime loan to a competitor when the security property changed hands. The new transferee would not want to forego the future value of such rights even for a lower interest rate elsewhere.

The mortgagee will have orderly repayment of his debt, strictly according to the repayment plan of this instrument without the attendant servicing costs that normally occur several times during the long-term present day mortgage.

Valuable time of the mortgagee will not be consumed by discussion and review of facts when an owner reports that he is temporarily unable to meet the mortgage terms as set up. Under the Plan, any forbearance that an owner is entitled to is clearly established and is obtainable by perfect payment performance. To exercise all or any part of his option to principal deferment the borrower need only notify the mortgagee, in writing, 10 days in advance of due date as to the required time.

Probably one of the outstanding advantages of the Plan is that it is applicable to existing business as well as new business and that the present portfolio of the mortgagee can be protected immediately with one or more retroactive benefits. In addition, a modest service fee may be charged to offset any expense that may be incurred.

Interest rates could be stabilized and the mortgagee would be able to earn a greater rate on his investments because new owners would be willing to pay above current rates for the protective features afforded by this new type repayment plan.

Foreclosures will be substantially reduced and consequently fewer losses will be involved because, for the most part, owners will be able to either rehabilitate themselves or realize something on their equity and place the mortgage in stronger hands during their earned and accumulated credit privileges. All of this is in contrast to present day mortgage provisions which give little or no rights to the mortgagor, and, as a result, when adverse times are upon the owner he immediately defends himself as best he can by milking the property or digging in, living out his equity and neglecting the property insofar as normal maintenance and care are concerned.

Automatic Extension

Immediately upon the exercise of any part of the right or rights to deferment of principal the loan becomes automatically extended for such desired earned period, but in no event beyond a maximum of 3 years. It would, therefore, be possible for a 12-year loan to become a 15-year loan, or a 15-year loan to become an 18-year loan where the eligibility to rights has been earned and fully exercised.

National banks, limited to 10-year loans requiring the monthly amortization of at least 40 per cent of principal, may apply the *Home Owners Safety Loan Plan* by accelerating the payments sufficiently to amortize 40 per cent of the debt within an 8 year period. This would allow two principal deferment periods during the life of the loan.

Amortized Feature Kept

In its simplest terms, the copyrighted Supplemental Agreement represents a rider to be attached to the lender's regular mortgage instrument without necessitating reprinting or disturbing such form of obligation. The Supplemental Agreement is designed to apply to both new and existing obligations and does not change any part of the mortgage instrument in present use except to modify the payment default proviso. It also incorporates an automatic extension feature in event any or all of the principal deferment periods are exercised by the borrower. Thus the amortized feature of the loan is not destroyed. It is still a loan that completely pays itself out during the original term or extended term of the instrument.

TWO CHAPTERS ISSUE NEW MEMBER ROSTERS

Two of MBA's progressive local chapters, Chicago and Southern California, have just published new membership rosters. Both are excellent and copies of each have been sent to other chapter presidents with the hope that if they haven't considered similar rosters they might profitably do so.

The Chicago roster lists all members, addresses, officers, committees and the code of ethics. The Southern California roster is somewhat more exhaustive and lists all officers, committees, member firms and, in addition, describes the business of each member. Institutional lenders represented by each member are also given. By-laws of the chapter is also reproduced. Chicago did not include its by-laws as was done in previous years because they are being revised and will be published later.

REPORT FROM TULSA

GRADUALLY rising farm prices during the remainder of the war followed by a sharp speculative drop of short duration when peace is declared and which, in turn, will be followed by a sharp inflationary rise lasting two years or more when price controls are released are the three most immediate developments to expect in the U. S. farm economy according to the prediction of Dr. E. C. Young, dean of the graduate school of Purdue University, speaking at our Tulsa Clinic. J. S. Corley, treasurer, Bankers Life Company, Des Moines, conducted the farm mortgage conference, featuring Dr. Young and Dr. E. C. Johnson of FCA.

The fourth development in the future pattern of six which Dr. Young said seemed most probable, was another sharp drop when demobilization is completed bringing considerable unemployment.

"This will be the most critical period in the determination of national policy," he warned.

The fifth development—if reconstruction is handled intelligently—should be a long period of reconstruction at home and abroad.

"During this period, farming should be profitable but probably in a relatively poor position compared to many other businesses. The livestock business, however, should be relatively good during this period," he said.

The sixth development—run-away inflation—is one he said need not occur but will occur if reconstruction is poorly handled.

Turning to the question of our food supply now and after the war, Young declared that "actually, it is difficult to increase the size of the farm plant because most of the good land is already in use. Farm buildings are generally adequate for the available land.

"Food production has increased about 16 per cent since the outbreak of war. Probably about half of the increase is attributable to the weather and half › more intensive farming."

Outlining his long-term view of the U. S. farm economy, Young declared that "events of the last 25 years demonstrate that the only final solution to the agricultural problem lies in the increased demand. If we can bring sufficient order into the world after the war so that people can find jobs at productive work, the agricultural problem will be a long way toward solution."

But he warned that "the United States has reached a stage in its development in which agricultural production will probably be inadequate if we have a prosperous expanding economy. The principal threats to an orderly and prosperous reconstruction period are run-away inflation and powerful economic pressure groups."

The city man is playing an important role in the current speculative land boom and while lenders ought to discourage the practice in every way they can when speculation is clearly indicated, they are pretty much at a disadvantage because city buyers of farms today are often paying all in cash, Dr. E. C. Johnson, chief, economic and credit research division, Farm Credit Administration, told the conference.

In some areas of the country, he said, city buying accounts for about a third of the farms being sold. He warned our farm members that it is their duty and responsibility to watch this trend carefully and be cautious about lending on farms purchased by city men who obviously can't make a success of farming.

Turning to present-day proposals to halt speculative transactions in farm land, he commented on the idea of taxing sales when the land is held for only short periods of time. The principal scheme already brought forward is the bill of Sen. Gillette of Iowa.

Johnson admitted that such a tax, if enacted, would be a curb on inflation but said he felt that lenders could, in a sense, make it unnecessary if they would refuse to lend on speculative transactions.

Johnson revealed a development which has received little public discussion when he said that there is evidence that farms in regions of low productivity have increased relatively more in price than farms in better areas. Farmers and lenders seemed to have made the mistake of generally over-valuing land in poorer farm areas.

High farm income, he declared, has been responsible for a great decline in farm debt. He estimated that the total farm mortgage debt has dropped from $6,586,399,000 on January 1, 1940 to about $5,650,000,000 on January 1st this year. Farmers are making

THE 1944 CLINICS

When the 1945 MBA Clinics are planned, you can be sure that the 1944 program will be studied and re-studied so that next year we can give members more of the same—but even better. Our Clinics this year met with a very favorable response and those for 1945 will be improved. Attendance at Tulsa totaled 168. Thirty-seven cities in fifteen states were represented by those registered. Highlight of the meeting was the unusually interesting and informative session on farm mortgages. Many members want to hear more of this type of discussion.

Attendance at MBA's three 1944 Clinics totaled more than 900. From our survey taken after the Chicago Clinic, we found that members liked the program in the ratio of about 60-to-4, that the vote was roughly 57 to 12 that Clinic programs should be devoted almost exclusively to shop talk and that members aren't especially interested in outside guest speakers. You who attended the Chicago Clinic voted 42 to 25 against luncheon meetings featuring speakers on international affairs, war experiences, etc. It all adds up to this conclusion: Members want practically nothing but discussions of the real, practical, every-day problems of running a mortgage business.

OVER 900 ATTEND 1944 CLINICS

more money and they are paying off their mortgages, which is a good thing, he observed.

This trend isn't all favorable, he added, because at the same time other farmers are going heavily into debt by additional purchases of land at high prices and "they are likely to experience difficulties when farm income decreases."

Private Capital's Job

"The mortgage business must be further modernized and streamlined," declared William Gill, vice president, American First Trust Company, Oklahoma City, in his address at the construction loan procedure session.

"The federal government should not further encroach on the real estate mortgage business—private capital, if left alone, can and should furnish sufficient funds on a basis equitable for the borrower and lender."

Aksel Nielsen, executive vice president, The Title Guaranty Company, Denver, said that in the past construction loans have been burdened down with too much cumbersome detail and declared that this type of financing in the future must be handled with the same ease as is the case with any other loan.

Homer C. Bastian, treasurer, Fidelity Investment Company, Wichita, Kan., and FHA director in Kansas from 1934 to 1941, outlined procedure followed in that state in building financing and said that after all safeguards have been set up, the operation is pretty much like everything else—a great deal depends on the individual case because they are all different.

Aubrey M. Costa, vice president, Southern Trust and Mortgage Co., Dallas, was the fourth speaker on the panel and described the methods used in his state. He declared he sees a great future in the construction loan field for mortgage lenders.

Residential building volume in the first postwar year was estimated at from 350,000 to 400,000 units averaging in cost about $5,000, with a total dollar volume of from 1¾ billion to 2 billion dollars by Franklin D. Richards, Washington, D. C., FHA commissioner for zone four, in his address.

Richards predicted that after the war the nation will have more equity money than it ever had before and that, by every means of charting the future, we will see a great upsurge in residential housing construction. Richards' estimate of the volume of building in the immediate postwar years is below the forecasts of many building economists whose predictions run as high as a million and a half residential units annually in the first postwar decade. The Richards' figures, however, are based upon scientific studies completed by FHA.

Richards held out no hope, however, that there would be much volume of private building soon. He said he believed there would be no resumption "until a successful termination of at least the European war."

He told the mortgage bankers and real estate men that FHA had made a very valuable contribution to the drive against inflation by refusing to recognize current inflated prices for real estate in its insuring operations. He further declared that it is highly advisable for lenders to finance a reasonable volume of the existing construction business under the FHA plan because it will help keep down inflation and abnormal prices and also enable the agency to maintain an organization ready to function in the postwar field.

Beware Inflated Values

A. A. Zinn, vice president, The State Life Insurance Company, Indianapolis, and a former MBA president, declared that in considering applications for loans today, he is particular to see that the applicant has not been too much influenced in his valuation by prices being paid now "under pressure buying by people who must pay exorbitant prices for homes in order to house their families."

"Watch you small corner neighborhood store values of your nondescript long-strong business street developments—they are in for trouble. In cities of 100,000 population and up, our retail distribution system is undergoing a radical change," declared Paul J. Vollmar, vice president, The Western and Southern Life Insurance Company, Cincinnati, in his address on business property loans.

"The blocks with stores on the first floor and apartments above are rapidly becoming obsolete. Be aware of this trend when analyzing their future," he warned.

"Entirely new suburban retail districts are being established although some are being rebuilt. The trend is toward new districts with restrictions that will provide ample community shopping but not so large that overdevelopment will occur to handicap the district," he said. "In the future these suburban developments will have ample off-the-street parking facilities and stores will have two entrances and two sets of show windows facing both the street and the parking areas. Sixty per cent occupancy will be by chain operators—many of the local type."

J. S. Corley, treasurer, The Bankers Life Company, Des Moines, spoke on apartment house loans and outlined the methods his company employs in considering loans on this type of property.

STANDARD LOAN FORMS FOR MEN IN SERVICE

Recently we noted that the Chicago MBA's FHA committee was working on a standard form which might be used for mortgagors in military service who request postponement of their principal payments. After a good deal of work, the Committee finally ended up about where they started and concluded that it doesn't seem possible to prepare such a form that would be acceptable to all different types of lenders. However, the Chapter does have available two sample forms now being used. The MBA national office will be glad to send them to any member who requests.

PEOPLE • CHAPTERS • EVENTS

With the Tulsa Clinic behind us, the heavy schedule of MBA meetings is over until the annual convention in October. The Executive Committee meets June 1st in Chicago and the Board of Governors the following day. Several other committee meetings are being planned for these days.

S. M. Waters, Minneapolis, chairman of the MBA farm loan committee, J. S. Corley, Des Moines, and Secretary George H. Patterson met with members of the National Agricultural Credit Committee in Chicago May 22 to discuss current problems in the farm credit field.

Donald C. Fitch, Travelers Insurance Company, Dallas, was elected president of the Texas MBA to succeed J. E. Foster, Jr., J. E. Foster & Son, Inc., Ft. Worth, at the annual meeting April 18 and 19 in San Antonio. The meeting was one of the most successful ever held in this chapter's series of 28 annual conventions. Guests from the National Association included President H. G. Woodruff and R. O. Deming, Jr., regional vice president. More than 150 attended.

A. H. Cadwallader, Jr., Mortgage Investment Corp., San Antonio; D. L. Treadway, Southland Mortgage Co., Dallas; and T. J. Bettes, T. J. Bettes Company, Houston, were elected vice presidents. Treadway and Cadwallader served in similar capacities last year. Alvin E. Soniat, J. E. Foster & Son, Inc., was named secretary and treasurer.

Under the guidance of MBA Past President Dean R. Hill, a reorganization of our Buffalo chapter is under way. The group hasn't been too active in recent years. First step in the plan was a luncheon meeting May 2 to which representatives of all important mortgage lending interests were invited. Twenty-two institutions responded. President H. G. Woodruff and Vice President L. E. Mahan made the principal talks. That evening Mr. Mahan addressed the Niagara Frontier Builders Association. In that address he pointed out that mortgage banking, which has grown to a twenty-eight billion dollar industry since the first World War, now stands ready to cope with the postwar problems which can be expected in our field.

"Private enterprise will be able to take care of all the mortgage financing needs for residential building and there is no need for government financing," he said and added that there are fewer delinquent mortgages now than at any time on record.

And speaking of local chapters, Donald T. Pomeroy, president, Pomeroy Organization, Inc., would like to see one in Syracuse and has already taken initial steps to see what can be done about it. If a local chapter can be organized there, Pomeroy is the man who can do it.

The name of the Tracy Loan & Trust Co., Salt Lake City, has been changed to Tracy-Collins Trust Co. to honor the president, James W. Collins, a former MBA president. In his letter announcing the change, Russel L. Tracy pointed out that Mr. Collins has been with the Company since he was 14 years old, has made a great contribution to its growth and success and that "I feel we should signally recognize and honor him in any way possible." The change in name was the result.

Detroit MBA's May meeting featured addresses by Raymond Foley, State FHA Director, who talked on Title VI vacancies and the relief situation, and A. J. Fushman of the RFC, who discussed current activities of his agency and its views on the war plant disposal problem.

Grant L. Miller, Omaha, Nebraska, representative of the farm mortgage of Penn Mutual, was elected president and secretary of the Nebraska MBA at the annual meeting and George Salladin, Lincoln, Nebraska, representative of the Mutual Benefit Life of Newark, was elected vice president. Miller succeeds Grover K. Baumgartner who has held office for several years. Twenty-six attended the meeting which was featured by a round table discussion of appraisals, interest rates and farm land values. Professor F. E. Keim, of the agronomy department of the University of Nebraska, outlined this year's annual short course which is sponsored by the University and our Nebraska chapter and which is one of the most important activities undertaken by any of our local associations. This year it will be in Lincoln, June 23.

C. Armel Nutter, MBA board member from Camden, N. J., heads the housing committee of the state's real estate association now making a comprehensive survey of public housing in New Jersey. The study is aimed at determining the cost of construction and maintenance of public housing, number of persons employed on operating staffs and other facts which will be helpful in making comparisons with privately-financed and privately-operated projects.

C. A. Legendre has succeeded the late J. P. Hogan as president of Standard Mortgage Corporation, New Orleans. Mr. Hogan was a former member of the MBA board. Charles W. Hogan, his brother, has been elected vice president.

Frank A. Weber, cashier, West Englewood, N. J. National Bank, and first vice president of the Northern New Jersey MBA, has been elected executive vice president of his bank.

BRIEFLY TOLD: M. T. MacDonald, Jersey City, substituted for Dean R. Hill as MBA's representative at the National Association of Manufacturers Postwar Conference . . . Kenneth W. Moore, Chicago Title and Trust Company, has been elected president of the Office Management Association of Chicago . . . Headquarters office visitors: S. M. Waters, Minneapolis, J. S. Corley, Des Moines, C. A. Legendre, New Orleans.

The MORTGAGE BANKER

Published Monthly at 111 West Washington Street, Chicago 2, by the

MORTGAGE BANKERS ASSOCIATION OF AMERICA

Herold G. Woodruff, *President* — L. E. Mahan, *Vice President* — George H. Patterson, *Secretary-Treasurer*

The Mortgage Banker is distributed free monthly to members of the Mortgage Bankers Association of America. Publications may reproduce material appearing in the magazine only by permission of the Association. Opinions expressed in The Mortgage Banker are those of the authors or the persons quoted and are not necessarily those of the Association.

JUNE, 1944

THE INFLATIONARY FACTOR IN LENDING

A good deal continues to be said and written about the dangers of inflationary real estate valuations. The latest organization to sound a warning is the Federal Savings and Loan Advisory Council of which our member, Walter Gehrke of Detroit, is secretary. These valuations "constitute a threat to the economic stability of many communities as well as to the safety of home ownership. The ability of financial institutions to supply credit for the resumption of large-scale home building after the war is also threatened," the Council said.

The developing "boom" is in part encouraged by inflationary mortgage lending, said the Council and urged all types of lending institutions to cooperate in combatting the danger. It recommended these precautions for adoption by all home-financing institutions:

(1) Downward adjustment of the ratio of loans to appraised values in order to assure that excess risks are covered by the down payment rather than by the mortgage loan. (2) Shortening of repayment periods. (3) Accelerated repayment of principal during the first few years of the loan. (4) Where possible, calculation of customary loan percentages on the basis of property prices in a pre-war period during which market conditions were reasonably stabilized. (5) The taking of additional security on loans, to consist of shares, government bonds, paid-up life insurance, or other collateral in cases where high percentage loans are made on the basis of current market prices.

WHAT MR. FERGUSON THINKS ABOUT IT

FHA Commissioner Ferguson also thinks the trend should be receiving our most careful consideration. Speaking the other day in Indianapolis, he declared that the best existing means of exerting influence against spiralling home prices is the FHA appraisal system, which is based on long-term values rather than short-term price increases.

"Through widespread use of the FHA system, the individual buyer can be made conscious of the fact that if he pays a high price for a property, he is paying a premium for immediate occupancy. At the same time, the lender is put on notice that the funds he is advancing may not be completely repaid and that he is taking a greater risk than prudence justifies."

If the situation is not met by FHA and interested groups, there will be strong pressure to continue price control measures, perhaps indefinitely, he said.

"In a completely uncontrolled situation, the mortgage and real estate markets could hardly escape sinking into a depression of long duration. With over-lending and over-buying at high prices, it is hard to see any result other than an ultimate crash with wholesale foreclosures, new mortgage moratorium laws, and a new HOLC to bail out the lending institutions."

While evidences of inflated prices on existing houses are already present, the situation is not yet so far out of line as to foretell inevitable collapse, Ferguson said.

"However, existing houses must be watched with particular care to avoid valuations and mortgage commitments that may be subject to deflation in the postwar period, and to avoid contributing to inflation."

HIS MIND NOT CHANGED

John H. Fahey hasn't changed his mind about selling the HOLC portfolio. The other day the agency sold all its loans in Hawaii to seven savings-and-loans. Reason: the difficult servicing problem for 266 loans 2,400 miles from the San Francisco office. Mr. Fahey took occasion to say that "The sale of these loans has no relation to the demands of some mortgage interests that they be permitted to buy all the HOLC loans in the country, by counties and States—at par for some mortgages and at large discounts for others. That scheme would result in heavy losses to the Government and no compensating advantages."

Purchasers of the Hawaiian loans are paying in cash the full unpaid balance of principal and interest on these mortgages plus a premium, without the necessity of reappraisals, or the assumption of any other responsibility or expense by the Corporation.

PROCESSING TIME CUT

Lenders who are complaining about the long processing time on FHA's should take a look at the record FHA has made for priority applications for building materials and equipment through the new WPB order P-55-c. A 73 per cent reduction in the average processing time required has been made. WPB order P-55-c simplifies priority procedures and authorizes FHA to approve applications without referring them to WPB.

For the week of January 28, before P-55-c became effective, the average processing time per priority application was 41 days. During the week of April 21, six weeks after FHA started using the simplified procedure, the average processing time was reduced to 11.1 days.

MORTGAGE OF TOMORROW

(Continued from page 1)

with which our members are most familiar is our proposal for the insurance of farm loans — something we have by no means given up as a lost cause.

Some other so-called new mortgage plans hardly seem to fill the bill. For example, a group of upstate New York banks announced a "new mortgage plan" which turned out to be nothing more than a willingness on their part to absorb appraisal, recording, attorney and other fees and charges.

All sorts of other ideas are being proposed but they can wait until another time. What all this has been leading up to is a specific plan called the *Home Owners Safety Loan Plan* which is the creation of a licensing organization under that name composed of men long experienced in the mortgage field. This plan has been discussed with many mortgage men, some of them MBA members. According to the sponsors, the plan has met with considerable favor.

It should be understood, of course, that MBA isn't sponsoring this plan or any other at this time. We are merely presenting it as an idea for consideration and discussion and we will welcome any comments from members. One thought is that it may stimulate other suggestions. It should be noted, too, that this plan is copyrighted and the explanatory article beginning on page two was prepared by the copyright owners for presentation here. Requests for further information should be addressed to the MBA national office and they will be referred to the sponsors.

This *Home Owners Safety Loan Plan* conception of the mortgage of tomorrow may appeal to you and if so we would like to hear why. Several have said that "the Plan has merit." Or, again, your reaction may be just the opposite. One MBA officer to whom it was shown said that his "personal reaction is that such a plan is wholly unnecessary. I do not believe that any mortgagee would foreclose at any time for amortization only. I am quite sure that the depression has taught mortgagees the wisdom of working along with distressed borrowers. But it is a subject that should be brought to the attention of members."

PRESIDENT'S LETTER

While the debate over inflated appraisals continues feverishly as ever, a few are venturing the opinion that, after all, nobody knows what the price level is going to be after the war and we might eventually find that some of these property valuations today won't be too high after all. Lenders who think this way are in the minority, but there are quite a number of them around.

Industry is just as interested in the problem as we are. Recently the economic research committee of Westinghouse made a study of the probable future price level, the first of its kind to be made, in fact. In brief, the committee found that American consumers can expect to pay from one-third to one-half more for goods in the postwar era than they did in 1940. This will be from 10 to 20 per cent above current prices.

As this is being written, I received an advance copy of Mr. Fahey's most recent statement in which he again warns of the inflationary trend. Some of his data is interesting. He said:

"While sale prices indicated by revenue stamps and mortgage recordings in recent months show plainly what is happening, the records of sales of houses by owners whose mortgages had been held by the HOLC reveal disquieting facts. During the first three months of this year, 1,293 properties owned by HOLC borrowers were sold at prices 17 per cent higher than the HOLC valuations made about ten years ago. On the average, these properties are now more than 20 years old. These new prices, of course, do not allow for depreciation or adverse changes in neighborhood conditions over the years.

"In connection with the sales of 4,097 properties on which mortgages were held by the HOLC, new loans were made by private institutions during the past 8 months showing an average loan increase of $1,504 per property, 81 per cent more than the balance owed on them when the HOLC loan was paid off.

"The records of HOLC indicate that inflationary sales are more common in and around Detroit, Milwaukee, Cleveland, San Francisco, Los Angeles, Seattle, Phoenix, Tucson, Evansville, Fort Wayne, Gary, and Hammond. Such sales are also numerous in Omaha, Lincoln, Little Rock, Louisville, Shreveport, Kansas City (Missouri), Oklahoma City, Tulsa, Houston, Salt Lake City and Seattle."

Members have been receiving our letters on the RFC Mortgage Company commitment matter. Before you receive this issue, you may likely receive another with later information. You have no doubt noted that the so-called G. I. bill has passed the Senate. Before we draw any final conclusions about it, we should wait to see what the final bill looks like after it emerges from conference. The House and Senate bills are considerably different.

Recently there has been an acceleration of public discussion about the number and kind of houses we must have after the war. Many members no doubt saw the newspaper versions of The Twentieth Century Fund's report on housing in which this organization concludes that "well over a million new dwellings a year of good quality could be used" and that the "majority of these should be medium-priced and low-priced, varying from $2,000 or even less in some regions to $4,000 and less in others."

The report itself offers some constructive suggestions; but when it holds out the possibility of livable decent homes for less than $2,000, I think the public is being deluded in believing that this is a reasonably attainable objective.

President, Mortgage Bankers Association of America.